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¶1. (U) Summary. This is Volume 8, issue 29 of U.S. Embassy Pretoria's South Africa Economic News Weekly Newsletter.

Topics of this week's newsletter are:
- OECD Thinks SAG Is too Dominant in Economy
- ANC Will Keep Inflation Targeting
- Crime Crippling Small Business
- SADC to Launch Free Trade Area
- Mercosur Trade Agreement Concluded
- U.S. Signs Trade and Investment Agreement with SACU
- SAA Optimistic Despite Posting Loses
- Kulula Irked by SAA Begging Bowl
- Quantas Bumps up SA Route
- Transnet Asserts that Eskom's Rating Should not Affect It's Expansion Plans
- Eskom Taps Former Gold-Miner Bobby Godsell as New Chairman
- Policy Release May Clear Way for Eskom Nuclear Power Plants
- SA's Engen Snaps up Shell's Business in Zimbabwe
End Summary.

OECD Thinks SAG Is too Dominant in Economy

¶2. (U) The Organization for Economic Co-operation and Development (OECD) said South Africa must do more to improve competition in its economy, and gives the state too big a role in tackling the constraints to growth. In its first report on South Africa, the 30-member group criticized the South African government's latest strategy for development, the Accelerated and Shared Growth Initiative for SA (ASGISA), saying that some of its policy responses were weak or inappropriate. Plans to give incentives to some industries to create more jobs would limit competition, while government programs and initiatives were "at odds with the recognition of failures of official planning, co-ordination and capacity" to achieve faster growth, the OECD-group said. The dominance of large private sector companies was also seen as negative, as this could be linked to lower output and employment, and higher prices. The OECD report praised South Africa for policies that have boosted economic growth, lowered inflation, and produced the country's first budget surpluses in history. At the same time, the report also highlighted what it saw as weaknesses stemming from high unemployment, poverty, the spread of HIV/AIDS,

and crime. "The most disappointing aspect of post-apartheid economic performance is the emergence and persistence of extreme levels of unemployment," it said. The report is a result of the OECD's drive to boost co-operation with emerging market economies that may want to join the organization in the future. Many of the OECD's conclusions appear to clash with plans by the African National Congress (ANC) to bolster the role of the state as it works to ease chronic poverty and income inequality. ANC President Jacob Zuma has said, for example, that the party wants to put the state right at the center of development, with a "critical role" for state enterprises. (Business Day, July 16, 2008)

ANC Will Keep Inflation Targeting

¶3. (U) African National Congress (ANC) Secretary-General Gwede Mantashe moved to calm investors' fears that a new ANC government would unleash an inflationary spiral by profligate state spending in favor of the poor. Government spending would be focused on
Qfavor of the poor. Government spending would be focused on investment rather than inflationary consumption spending, and the question of a budget surplus or deficit would have to be linked to the state of the current account of the balance of payments, Mantashe said. Budget surpluses were not a curse as such, he said, but were unacceptable if they arose from the state's inability to spend. He dismissed fears that the post-Polokwane ANC leadership was a group of "leftist, low-caliber individuals" who posed a risk to the solid foundations built up over the past 14 years. Mantashe strongly supported the continuation of the policy of inflation targeting, but urged that the target band be debated. He believed monetary policy should not focus only on inflation but also on social issues such as unemployment. He said it would be "disastrous" if land redistribution jeopardized agricultural production, saying the policy should not be pursued simply to

achieve the 30% land transfer target by 2014. The rural poor should be helped to become more self-sufficient in food production and less dependent on social grants because "the grant regime is not sustainable in the long term." At the same time, Mantashe stressed the need for a greater focus on job creation and social services to prevent the alienation of the poor. Mantashe said the 2009-10 medium-term budgetary framework would focus on accelerating the pace of economic growth and investment in productive capacity, job creation, development of a social security net, and improving the capacity and effectiveness of the state, especially in fighting crime. (Business Day, July 17, 2008)

Crime Crippling Small Business

¶4. (U) A study commissioned by the South African Presidency found that a quarter of South Africa's small businesses were reluctant to expand or employ more people after having been exposed to crime. The smallest, most vulnerable companies and the most successful entrepreneurs were the hardest hit. It was estimated that smaller businesses could expect to lose at least 20% of annual turnover to crime through direct and indirect costs, which could mean the difference between the survival and failure of a small company. Half of the companies interviewed had no insurance. The findings have serious implications for the government's economic growth and job creation plans, which hinge largely on the development of a small business sector that the government believes has the potential to lift millions out of poverty and into the mainstream economy. The survey found that businesses directly affected by crime were 20% less likely to increase their staff numbers, and were 10% were more likely to shed jobs, with those in informal settlements or townships the most vulnerable. The survey recommended that more effective policing be provided, with greater co-operation among business and the police, particularly in the townships and informal settlements. It also recommended that the Department of Trade and Industry develop mechanisms to assist emerging businesses, such as subsidies for burglar- proofing. (Business Day, July 17, 2008)

SADC to Launch Free Trade Area

¶5. (U) The Southern African Development Community (SADC) is set to launch a Free Trade Area (FTA) on August 17. However, integration is not limited to creating an FTA. The strategic plan of SADC, as set out in the Regional Indicative Strategic Plan (RISP), foresees a customs union in 2010, a common market by 2015, a monetary union by 2016, and a single currency by 2018. SADC private sector representatives recently met to discuss the implementation of the SADC FTA and the ambitious plans for deeper economic integration. Although the private sector participants strongly supported the promotion of intra-SADC trade and investment, they agreed that it is unrealistic to introduce a customs union until the FTA has been fully and successfully implemented. Private sector organizations from eleven of the fourteen member states were in attendance, but
Qfrom eleven of the fourteen member states were in attendance, but
the representatives held different views on how to achieve an optimal integrated market. South African representatives were primarily focused on exporting products to the rest of SADC as efficiently and cheaply as possible. In contrast, representatives from the rest of SADC were less concerned about trade facilitation and more about supply side capacity required to create the right environment for their manufacturing industries. (Tralac Newsletter, July 16, 2008)

Mercosur Trade Agreement Concluded

¶6. (U) The Southern African Customs Union (SACU) has concluded a preferential trade agreement with Mercosur, which includes Brazil, Argentina, Uruguay and Paraguay. According to SA's Chief Trade Negotiator Xavier Carim, all technical negotiations have been concluded. The agreement will be submitted to the national authorities to ensure legal conformity to national laws. A date will then be determined for ministerial signature and ratification. It is not a free trade agreement, but creates a legal framework for trade in goods between SACU and Mercosur. The agreement covers

2,000 products. An agreement was built into the pact that allows the parties to expand the trade agreement should they wish to do so. (The South African Exporter Supplement, Business Day, July 2008)

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U.S. Signs Trade and Investment Agreement with SACU
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¶7. (U) The Southern African Customs Union (SACU) has concluded a trade, investment and development co-operation agreement (TIDCA) with the U.S. The pact is not a free-trade agreement. However, South Africa's Chief Trade Negotiator Xavier Carim said the deal was important as the parties would look to co-operate on sanitary and phytosanitary (SPS) issues and other technical areas. In terms of the agreement, technical barriers to trade would be identified, and the parties would attempt to facilitate trade in those areas and pursue investment promotion activities. SACU already has preferential access into the U.S. market under the unilaterally extended African Growth and Opportunities Act (AGAO). (The South African Exporter Supplement, Business Day, July 2008)

SAA Optimistic Despite Posting Loses

¶8. (U) South African Airways (SAA) has posted a net loss of R1.09 billion ($142 million) for the 2007/08 financial year. The loss is attributed to once-off restructuring costs of R1.35 billion ($175 million) and a 1.3% decline in passenger volume. CEO Khaya Ngqula asserted that this is a good result considering that SAA decreased its capacity by 30% when it grounded six of its aircraft. Ngqula also said the airline has done extremely well when compared to the performance of the global airline industry. He emphasized that SAA

is currently above target in the current financial year, and although it will be tough, he is confident a profit will be achieved. (Travel Hub Report, July 17, 2008)

Kulula Irked by SAA Begging Bowl

¶9. (U) Low-cost airline Kulula lamented to the press that it is fed-up with South African Airways (SAA's) continued requests for the South African government to recapitalize the state-owned airline. Kulula said that in the past few years the government had poured more than R15 billion into SAA, which most recently requested a further R6 billion (R2.8 billion of which it has already received in the form of a loan). Following the release of yet another disastrous set of results from SAA, Kulula once again called on the SAG to keep promise made by the Minister Public Enterprises last year that "taxpayers will stop filling the begging bowl for ailing state-owned businesses." Kulula said there were more pressing needs, such as education, health, safety and security. Kulula pointed out that "South African aviation is littered with failed airlines that could not compete with state-funded SAA - Flitestar, SunAir and Nationwide to name just three, and state re-nationalization of the industry will continue to be destructive to free and fair competition." The airline also referred to the recent OECD report, which highlighted excessive state involvement in Qrecent OECD report, which highlighted excessive state involvement in the economy, and its constraining effect on growth. The airline said it was bizarre that Comair, which runs Kulula, paid hundreds of millions of rands a year in income tax, fuel taxes, value added tax, import duties and other levies, only to have this paid over to SAA to compensate for its inefficiencies. (Business Day, July 18, 2008)

Quantas Bumps up SA Route

¶10. (U) Quantas Airways announced that its South African service is unlikely to be affected by the airline's recently introduced cost-cutting measures, since both its Perth and Sydney routes were performing well. Quantas Manager for Africa Michaela Messner said there is a strong demand for both corporate and leisure travel, with yearly growth on both routes out of Johannesburg. Quantas plans on increasing its service on the Sydney route by adding a sixth flight to its weekly schedule in December. The decision to add the additional flight was a result of strong demand for its newly

launched Premium Economy Class product. Messner noted that the premium product appealed to passengers who "look to travel in comfort but are not able to afford business class." (Travel Industry Review, July 2008)

Transnet Asserts that Eskom's Rating
Should not Affect It's Expansion Plans

¶11. (U) State-owned transport and freight logistics group Transnet announced that foreign investors are sufficiently discerning to be able to distinguish between the financial health of Transnet and state-owned power company Eskom. Transnet asserted that its ability to raise capital should not be undermined, even if Eskom's credit rating were to be downgraded. CEO Maria Ramos will embark on an international road show to engage with the credit rating agencies, potential investors, and key export credit agencies. Ramos acknowledged that the tightening in the capital markets did coincide with a crucial debt-raising year for Transnet, which would be seeking to raise nearly R37 billion ($4.8 billion) over the next three years. She said that there was still considerable appetite for well managed, emerging-market infrastructure companies. "There are still investors out there looking for good infrastructure assets. But it will take careful planning as people will be looking at the quality of the credit more carefully, whereas a year ago it seemed no-one looked at anything and money was being thrown at you,"

she explained. For now, the credit-ratings agencies have maintained their respective negative outlooks on Eskom, but none had moved to downgrade the power utility. By contrast, Ramos noted that Transnet's rating had improved in recent years and that it had issued its first bonds without resorting to government guarantees. CFO Chris Wells stressed that, despite current financial-market stress and illiquidity, the group would press ahead with its plan to raise funds from both the domestic and international capital markets. The largest portion of the debt would be raised domestically. "Importantly, though, we are going to need to raise money on foreign markets, and we have estimated that it could be 26%," Wells said. He cautioned that the percentages could change depending on where it would be most cost effective to raise the finance. Transnet's three-year timetable indicated that it would have to raise R13.7 billion ($1.8 billion) in the current financial year to help fund the R20 billion ($2.6) in capital expenditure the company has already budgeted for. That figure should rise modestly to R13.8 billion ($1.8 billion) in 2010, before falling to around R9 billion ($1.2 billion) in 2011.

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Eskom Taps Former Gold-Miner Bobby Godsell as New
Chairman DTI Launches Rural Tourism Promotion Scheme
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¶12. (U) Well-known business and mining personality Bobby Godsell was appointed Eskom Chairman at the state power company's annual general meeting on July 17. The former AngloGold Ashanti CEO will replace the embattled Valli Moosa, who has taken criticism for the power
Qthe embattled Valli Moosa, who has taken criticism for the power
crisis in South Africa. Godsell currently serves as chairman of Business Unity SA and was formerly president of the Chamber of Mines. His appointment follows the recent appointment of another prominent mining figure to catalyze change at Eskom -- former Kumba (Iron mining company) CEO Ras Myburgh will advise Eskom on coal procurement. A Business Day editorial welcomed the sorely-needed injection of leadership at the power company, citing Godsell's experience as a high caliber, tough manager who can apply needed attention to detail. Speaking at a recent conference on the electricity crisis, Godsell called for a "Team SA" approach to dealing with the crisis, asserting, "This is a national crisis and we need a national effort to respond to it. There is no point in having the cheapest electricity in the world if you don't have any electricity. The challenge now is whether our leadership can be both cohesive and decisive in the way it was in 1994. We've had too many summits about the crisis; it's time to get on with it." (Engineering News, Business Day, Sunday Times, July 13-18, 2008)

Policy Release May Clear Way for
Eskom Nuclear Power Plants

¶13. (U) Department of Minerals and Energy Chief Director of Nuclear Energy Tseliso Maqubela said Minister Buyelwa Sonjica would shortly launch the new nuclear energy policy which was adopted by the cabinet last month. Maqubela said the major change between the final policy (not yet released) and the draft released for public comment last August (available on the SA DME web-site at http://www.dme.gov.za/energy/documents.stm) was the removal of a proposal to set up an agency devoted to nuclear security. He said this function should be performed by the national nuclear regulator, in line with international practice. "Nothing has really changed except the wording in some cases to indicate that nuclear will not be the only energy developed," Maqubela said. Flexibility has been built into the policy approach to accommodate the development of new technologies and changing market conditions. Maqubela said that it was no longer the case that the South African government had quantified a fixed target for nuclear of 25% of total power generation by 2025-2030 (from existing 6%). "We don't want to tie ourselves down - it could be that clean coal technology or methods for carbon capture and storage are developed," he added. Eskom is assessing bids from Westinghouse and Areva for construction of the first 3,000 MW tranche of a new nuclear power plant, but the

decision on the preferred supplier has been deferred to September from June. Meanwhile, the government has enlisted the aid of a brand consultant, Freedthinkers, to give the image of nuclear power in South Africa a make-over and attempt to unearth and correct misperceptions and apprehensions on the part of the public. Opponents fear that the move may be an attempt to short circuit public consultation as the government presses ahead with its program to build up to a dozen more conventional plants and potentially twice that number of pebble-bed modular reactors. (Engineering News, Business Day, Business Report, July 11, 14, 2008)

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SA's Engen Snaps up Shell's Business in Zimbabwe
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¶14. (U) SA petroleum products group Engen announced it had concluded a sale and purchase agreement to buy Shell's downstream business interests in Lesotho and crisis-torn Zimbabwe, where Engen said it was taking a long-term view that the economy would recover. Engen has also recently acquired Shell's downstream interests in Gabon and the DRC. Engen's spokeswomen said the recent acquisitions were in support of the company's increased focus on sub-Saharan Africa. In Zimbabwe, Engen - owned by Malaysian oil company Petronas (80%) and black economic empowerment group Worldwide Africa Investment Holdings - would purchase Shell's share in a joint venture with BP. Engen CEO Rashid Yusuf said, "While Zimbabwe's economy has declined sharply over the last decade, it still has good infrastructure which we believe will form the basis of renewed economic growth, once the current political situation is resolved." A Shell spokesman said the deals were consistent with the multinational's "more upstream and profitable downstream strategy, and the company remains
Qand profitable downstream strategy, and the company remains committed to Africa." (Business Day, July 11, 2008)

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